

## Transport & Logistic

### Stormy Waters, No Land in Sight

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**NEUTRAL**



We have downgraded our sector call from OVERWEIGHT to NEUTRAL on the back of: (i) higher uncertainties in the global shipping market despite more manageable vessel supply due to an expected weak trade demand in 2015, (ii) headwinds in port industry on possible hiccups caused by GST implementation, and (iii) less attractive valuations of big-cap shipping and port players under our coverage due to strong share price YTD performance. One potential positive catalyst is the impending container tariff ceiling hike in Port Klang, but we have not factored into our forecast due to uncertainties in timing and quantum of the increase. Volatility continued to persist in the shipping segments with the Petroleum tanker segment remaining strong while Dry Bulk segment was weaker-than-expected due to the absence of iron ore restocking by China on a similar scale in 2013. At the moment, we prefer small to mid-cap stocks like SURIA (OP; TP: RM3.41) and HARBOUR (OP; TP: RM2.20) on the back of their growth stories driven by Jesselton Quay development in Kota Kinabalu port and SCORE initiative by the Sarawak government, respectively. Meanwhile, we have downgraded WPRTS (UP; TP: RM3.13) from OP to UP with TP maintained.



**Port industry unexciting amid GST implementation, but weaker MYR could bring positive effects.** Upon the expected implementation of GST in 2015, import activity is poised to be weaker due to knee-jerk reaction by local consumers. While demand is expected to normalise months after the implementation, we expect growth in container throughput handled by port operators to be mediocre in 2015. Meanwhile, further weakening of MYR could have some positive impact on Export throughput which will partially mitigate the anticipated decline in Import throughput.

**Port Klang impending tariff hike not factored in yet.** Talks of Port Klang Authority rising the tariff ceiling for port operators based in Port Klang has been around for years and until now timing of implementation remains unknown. The tariff ceiling upwards revision will not translate into a linear positive increment in revenue for the port operators as some of them may be charging their core clients at lower rates than the

ceiling tariff. We expect port operators with higher Import/Export throughout weightage to benefit more from the tariff ceiling increase as Import/Export cargoes are less price elastic as compared to transshipment throughput. We believe a tariff ceiling hike is imminent despite timing uncertainty given that the tariff ceiling has not been lifted for 10 years despite rising fuel and electricity cost. However, we are not factoring in any potential impact from the tariff ceiling revision due to uncertainties in timing of implementation and quantum of the increase.

**More volatility in the shipping segment.** Petroleum tanker segment extended their strong performance as slower vessel supply growth reduced the surplus gap in the market. Meanwhile, dry bulk shipping rates have fared worse than expected with bigger sized vessels taking a bigger hit as China did not restock iron ore inventory aggressively in contrast with the corresponding period last year, inducing lesser demand for dry bulk trade. Chemical tankers remained flattish while LNG tanker segment's weak performances persisted amid impending supply overhang of vessels. While we anticipate a better year for the shipping industry overall as vessel supply slows, volatility in rates are expected to persist and sustainability of increase in rates hinges on the growth in demand for global trade, which remains uncertain in the meantime amid slowing growth in China economy and uncertainties in US and European economies.

**Downgrade sector to NEUTRAL, mid-small cap still preferred.** Since our previous sector report, WPRTS has posted robust capital gains to date (WPRTS: 30.8%), bringing its valuations to a less attractive level. Therefore, given the less attractive valuations and more uncertainties expected in both the shipping and port industry for the year ahead, we have downgraded our sector call from OVERWEIGHT to NEUTRAL. For the stocks under our coverage, we have downgraded WPRTS from OP to UP with TP maintained. For now, we prefer small and mid-cap counters in our logistics universe namely SURIA (OP; TP: RM3.41) and HARBOUR (OP; TP: RM2.20) underpinned by expected positive impact from Jesselton Quay and SCORE initiative, respectively coupled by their attractive valuations, which are standing at FY15 PER of 10.1x and 3.9x respectively.



**Comments on shipping rates****Petroleum & chemical tanker closing rate comparisons**

	3Q14	2Q14	QOQ change (%)	3Q13	YoY change (%)
VLCC	28,500.0	24,000	18.8%	18,000	58.3%
Suezmax	23,000.0	20,000	15.0%	15,500	48.4%
Aframax	18,000.0	15,750	14.3%	12,250	46.9%
LR2	18,000.0	15,750	14.3%	16,000	12.5%
LR1	15,750.0	15,250	3.3%	14,750	6.8%
MR	14,000.0	14,250	-1.8%	14,250	-1.8%

Source: Fearnleys Research

**Petroleum remained strong with chemical rates flattish.** On QoQ basis, petroleum tankers performed relatively well with double-digit growth registered on the back of higher volume as a result of seasonality. Strength in rates was more significant on YoY basis with all VLCC, Suezmax and Aframax rates growing by 58.3%/48.4%/46.9%, respectively, on the back of better equilibrium between supply and demand of vessels. Movement in rates appeared to be uneven across the segments with larger-sized LR2 tanker rates achieving double-digit QoQ and YoY growth while LR1 and MR tankers' rate were flat. This indicated that cargo volume was higher in longer-haul West Africa to United States and Europe routes compared to shorter routes; for instance the Intra-Asia route which generally requires LR1 or MR product tankers.

**Drybulk tanker closing rate comparisons**

	3Q14	2Q14	QOQ change	3Q13	YoY change
Capesize (150k DWT)	14,000	14,500	-3.4%	17,500	-20.0%
Capesize (170k DWT)	17,000	19,000	-10.5%	22,000	-22.7%
Panamax (75k DWT)	9,500	8,750	8.6%	12,800	-25.8%
Handysize (53K DWT)	11,500	10,500	9.5%	10,250	12.2%

Source: Fearnleys Research

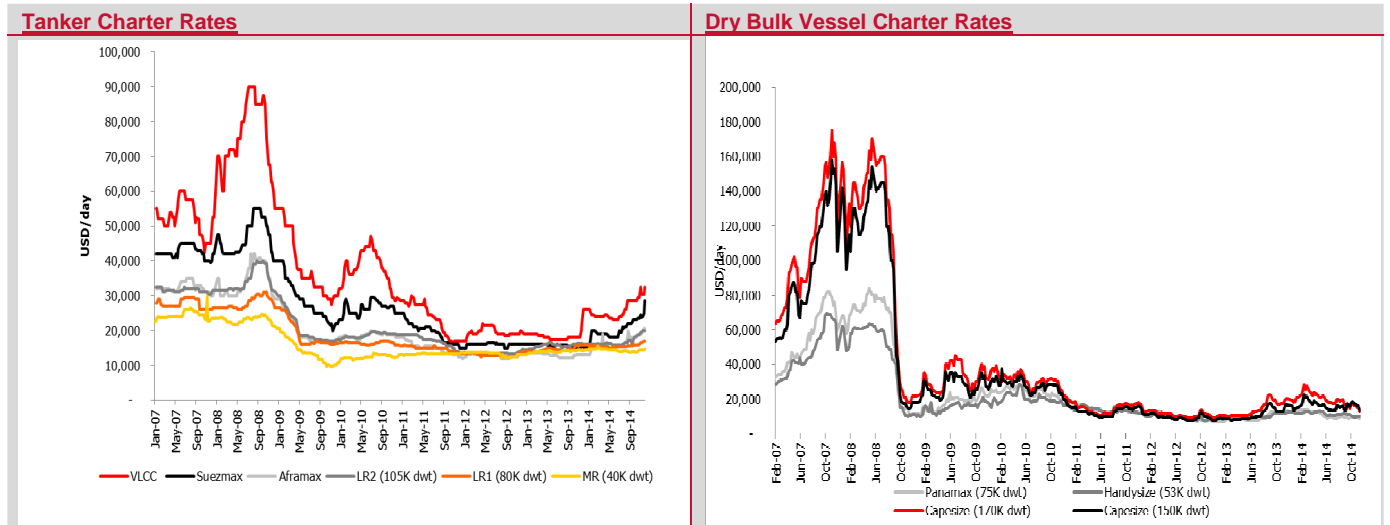
**Dry bulk disappointing in absence of iron ore restocking by China.** Charter rates for the dry bulk segment underperformed as opposed to our earlier bullish expectations with bigger-sized vessels experiencing weaker rates as compared to rates achieved in the previous quarter and corresponding period last year. This was mainly due to the absence of aggressive restocking of iron ore by China unlike last year which boosted demand for bulk trade significantly. Meanwhile, smaller sized vessel, namely Handysize vessel managed to garner positive increment on both QoQ and YoY basis, underpinned by lower vessel oversupply pressure in the global market as a result of slowdown in ship-ordering activities.

**LNG tanker closing rate comparisons**

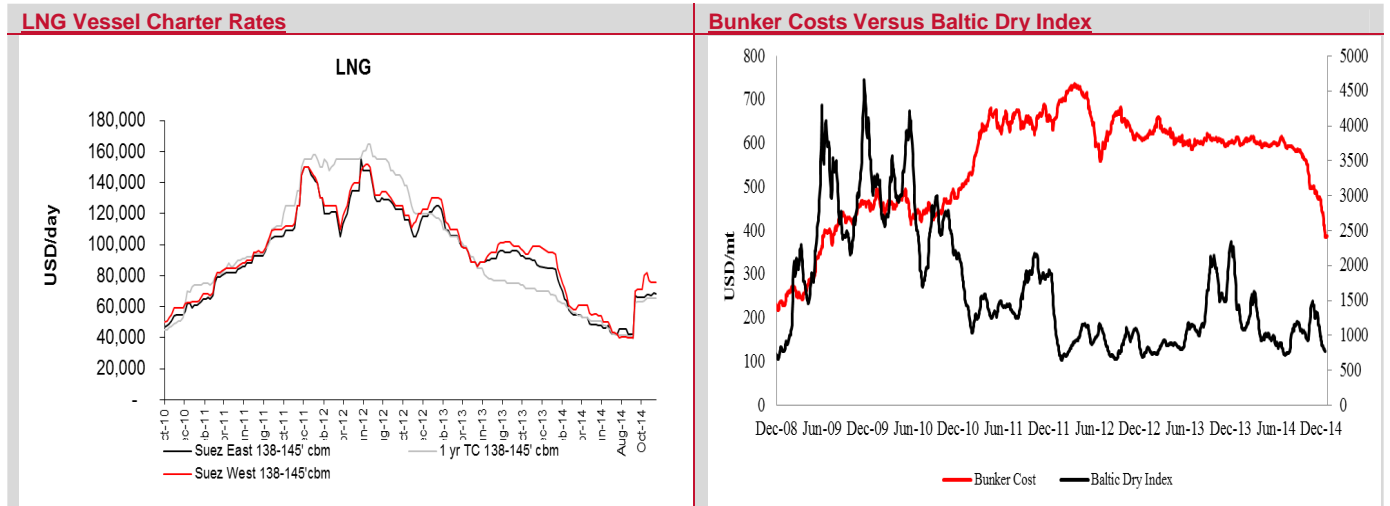
	3Q14	2Q14	QOQ change	3Q13	YoY change
Suez-East	42,500	46,000	-7.6%	96,000	-55.7%
Suez-West	40,000	50,000	-20.0%	99,000	-59.6%
1-yr TC	39,500	48,000	-17.7%	75,000	-47.3%

Source: Fearnleys Research

**Weak LNG spot market as expected.** LNG spot and 1-year time charter rates continued to weaken further on the back of vessel supply overhang in the global LNG market. However, a significant portion of existing LNG contracts are long-term in nature (20 years) with rates at significant premium to spot rate and only the current vessels on fast-expiring LNG contract are going to be hit by the slump in LNG spot market.



Source: Fearnley's Research, Kenanga Research



Source: Fearnley's Research, Kenanga Research



30 December 2014

### Peer Comparison

Company Name	Price (19-Dec-2014)	Mkt Cap	Core PER (x)			Est. Div. Yld.	Historical ROE	P/BV	Core Net Profit (RMm)			This Year Growth	Next Year Growth	Target Price	Rating
	(RM)		(RMm)	CY13A	CY14F				CY15F	(%)	(%)				
<b>CORE COVERAGE</b>															
BIPORT	7.00	3,206.2	20.4	23.1	20.2	3.4%	22.2	3.0	157.9	139.5	159.4	-11.7	14.3	8.08	OUTPERFORM
MISC	7.24	33,210.6	21.4	19.8	16.9	0.6%	3.6	1.3	1,513.2	1,631.9	1,908.1	7.8	16.9	7.49	UNDERPERFORM
WPRTS	3.31	11,253.0	25.9	23.8	22.4	3.2%	25.6	7.0	435.3	474.2	503.8	8.9	6.2	3.13	UNDERPERFORM
INTEGRA	2.29	694.9	16.9	19.5	15.7	1.5%	7.2	1.1	40.9	35.3	43.9	-13.6	24.4	2.47	MARKET PERFORM
MAYBULK	1.17	1,360.0	26.2	71.3	18.8	0.6%	3.8	0.7	44.6	16.4	62.4	-63.2	280.5	2.50	OUTPERFORM
HARBOUR	1.45	294.8	8.2	7.6	3.9	1.4%	10.6	1.3	32.2	34.6	67.0	7.5	93.9	2.20	OUTPERFORM
NCB	2.28	1,236.8	20.8	238.3	195.0	1.4%	9.9	0.8	51.6	4.5	5.5	-91.3	22.2	1.83	UNDERPERFORM
SURIA	2.30	719.7	10.6	10.3	10.1	3.2%	6.5	0.8	61.3	63.4	64.7	3.4	2.1	3.41	OUTPERFORM

Source: Bloomberg, Kenanga Research

**Stock Ratings are defined as follows:**

**Stock Recommendations**

- OUTPERFORM : A particular stock's Expected Total Return is MORE than 10% (an approximation to the 5-year annualised Total Return of FBMKLCI of 10.2%).
- MARKET PERFORM : A particular stock's Expected Total Return is WITHIN the range of 3% to 10%.
- UNDERPERFORM : A particular stock's Expected Total Return is LESS than 3% (an approximation to the 12-month Fixed Deposit Rate of 3.15% as a proxy to Risk-Free Rate).

**Sector Recommendations\*\*\***

- OVERWEIGHT : A particular sector's Expected Total Return is MORE than 10% (an approximation to the 5-year annualised Total Return of FBMKLCI of 10.2%).
- NEUTRAL : A particular sector's Expected Total Return is WITHIN the range of 3% to 10%.
- UNDERWEIGHT : A particular sector's Expected Total Return is LESS than 3% (an approximation to the 12-month Fixed Deposit Rate of 3.15% as a proxy to Risk-Free Rate).

**\*\*\*Sector recommendations are defined based on market capitalisation weighted average expected total return for stocks under our coverage.**

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